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IMPLICATIONS OF AN INCREASE IN US-SOVIET TRADE

Submitted by the

DIRECTOR OF CENTRAL INTELLIGENCE

The following intelligence organizations participated in the preparation of this estimate: The Central Intelligence Agency and the intelligence organizations of the Departments of State, the Army, the Navy, the Air Force, and The Joint Staff.

Concurred in by the

UNITED STATES INTELLIGENCE BOARD

on 7 October 1958. Concurring were The Director of Intelligence and Research, Department of State; the Assistant Chief of Staff for Intelligence, Department of the Army; the Director of Naval Intelligence; the Assistant Chief of Staff, Intelligence, USAF; the Director for Intelligence, The Joint Staff; the Assistant to the Secretary of Defense, Special Operations; and the Director of the National Security Agency. The Atomic Energy Commission Representative to the USIB and the Assistant Director, Federal Bureau of Investigation, abstained, the subject being outside of their jurisdiction.

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IMPLICATIONS OF AN INCREASE IN US-SOVIET TRADE

THE PROBLEM

To estimate the implications within the Bloc and the Free World of an increase in US-USSR trade.

CONCLUSIONS

1. The Soviets probably genuinely desire an increase in US-USSR trade. The possibilities for expanding this trade are severely restricted, however, by the limited range of Soviet goods likely to be marketable in the US, by US administrative and legislative measures in the fields of commercial policy and economic defense, and by the uncertainty of private US business reaction. We believe it reasonable to assume that if the US were to modify certain administrative restrictions, especially export licensing, US export to the USSR might expand over the next few years to about $100–150 million annually. While the USSR would probably not be able to balance trade at this level by its own direct export of goods to the US, it could make up the residual amount by reexports, transfers of free exchange, and by selling more gold to the Free World. *(Paras. 5, 7, 9, 14)*

2. An increase in imports from the US of the volume and composition postulated in this estimate would have little impact on the Soviet economy. The consumers goods industry could benefit the most if the Soviet leaders so decided; in some cases, however, the imported machinery and equipment could be used to increase the output of commodities for use in more basic industry. Assuming US control on the export of strategic goods, we believe the postulated increase in trade would have little effect on Soviet military potential. Soviet trade with underdeveloped countries or Communist China would not be significantly affected. *(Paras. 15–20)*

3. The Soviet leaders probably believe that increased trade with the US would strengthen their line of peaceful coexistence, diminish US ability to maintain Western trade controls and a generally strong anti-Communist position, and create frictions in the West as various countries found themselves in competition with the US for Soviet trade. We do not believe that these developments would occur to a significant degree. Most non-Communist countries would favorably view an increase in US-USSR trade as a sign that world tensions were relaxing. This would not be true of South Korea and Nationalist China, however, or among

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some elements in other countries. Japan, as well as many underdeveloped countries, would become less receptive than they are today to US advice against expanding economic relations with the Bloc. *(Paras. 8, 21)*

4. In the final analysis the view taken by most countries would depend largely upon the impact which increased US-USSR trade had upon the trade of those countries. It is possible that certain countries would be adversely affected by US competition in the Soviet market or, more probably, by an increase in Soviet raw material exports to the US. We believe that at the postulated levels of trade such effect would in general be small. Nevertheless, substantial increase in US imports of certain specific commodities from the USSR might seriously damage the trade or the foreign exchange position of particular Free World countries. *(Paras. 21–23)*

DISCUSSION

I. INTRODUCTION

5. The possibility of a substantial increase in US-USSR trade was raised by Khrushchev's letter to President Eisenhower, 2 June 1958. Khrushchev proposed that the USSR would buy non-strategic industrial equipment, especially for the production of synthetic materials and consumer goods, and would sell to the US in return basic commodities, including manganese and chrome ore, asbestos, lumber, furs, and possibly some machinery and equipment of modern design. To accelerate the expansion of trade, he suggested that the US provide long term commercial credits. He also proposed the conclusion of licensing agreements, exchange of technical information, and an inter-governmental agreement to regulate economic relations between the two countries.

6. Khrushchev's proposal, although generally businesslike in tone, was probably in the first instance a propaganda gesture. Whether or not it was accepted, it would further the Soviet line of "peaceful coexistence" by appearing to respond positively to US proposals that world trade be increased. It asserted that US industry would be interested in getting orders "now," an obvious reference to the US recession, the impact of which has been overestimated by the Soviets. Moreover, the fact that Khrushchev referred to trade in the "billions" demonstrates the propaganda aspects of the note. He is certainly aware that the Soviet Union does not have exports sufficiently attractive to the US market to support trade at such a level; he must also be aware that there is only the most remote chance that the US, in present circumstances, would extend large and long term credits to the USSR.

7. Nevertheless, we believe that the Soviet Union genuinely desires an increase in its trade with the US — a trade which in 1957 comprised exports to the US of $16.8 million and imports from the US of only $4.5 million. The Soviet effort to strengthen its industrial base and to increase the availability of consumer goods would be facilitated by obtaining technologically advanced machinery and equipment from the US, e.g., for the petrochemical and plastic industries. The Soviets would thus avoid some of the costs of development, and, as Khrushchev pointed out to the Central Committee in May 1958, could save much time by importing plant from the US, UK, and West Germany. If in addition, they could obtain long term US credits, they could acquire the facilities to increase production with a minimum initial drain on their own resources.

8. The Soviet leaders almost certainly also believe that important political gains would flow from a substantial increase in Soviet trade with the US. In their view, it would be likely to strengthen the Moscow line of peaceful

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coexistence and to weaken the effectiveness of US efforts to maintain a strong anti-Communist position. The Soviet leaders probably believe that such a development would further diminish the US ability to maintain Western trade controls. They may also think increased trade with the US would create divisive frictions in the West as other Western industrial countries observed the US increasing its share of the Soviet market.

II. POTENTIAL MAGNITUDE OF US-USSR TRADE

9. Despite Soviet desire to expand US-USSR trade, it is difficult to estimate the extent to which this trade might realistically be expected to increase, and to judge the permanence of such an increase if it were to occur. The primary factors involved would be the ability of the Soviet Union to make available for export commodities which could be sold in the US, the willingness of the US government to relax legal and administrative discriminations against trade with the USSR, and the willingness of private US industry to do business with the Soviet Union.

10. Judging by the Soviet goods which we believe potentially available for export to the US, it is almost certain that the Soviet Union would have difficulty in increasing its exchange earning capacity. The US now obtains from non-Communist sources virtually all its imports of the raw materials mentioned by Khrushchev. Further, for manganese and chrome in particular — at one time major Soviet exports to the US — many of the new sources to which the US has turned have been developed by US private and government capital, and supplies appear ample. While the USSR could undercut existing prices of these materials, it would have to be wary of charges of dumping, which could result in additional US restrictions. While the Soviet leaders would probably be willing to sell some types of machinery in which they have made innovations, there would not be enough of such items to yield a significant return. The Soviets would be unlikely to make the effort necessary to market ordinarily competitive types of machinery and equipment in quantity to US importers.

11. Existing US measures tending to restrict US-USSR trade also pose a formidable obstacle to any increase in such trade. Congress has enacted laws under which the import of crabmeat and certain furs of Soviet origin is prohibited and most-favored-nation (MFN) tariff treatment is specifically denied the Soviet Union, thus depriving it of the tariff benefits negotiated since 1934. The lack of MFN tariff treatment would be a most significant obstacle to US imports of manganese ore and ferroalloys from the USSR. More important, perhaps, it would hinder US imports of Soviet goods which have not historically been part of US-USSR trade but which would probably have to enter the trade to finance a really substantial volume of Soviet purchases here. The USSR and other communist countries also place a high symbolic value on MFN treatment and would undoubtedly make it a major objective in any trade negotiations with the US. US export controls continue to be more stringent than those recently agreed to by the members of COCOM. Finally, the Battle and Johnson Acts prohibit governmental and private loans to the USSR; under present legal interpretations US exporters or banks could grant no more than 180-day commercial credit to the Soviet Union.

12. Even if the US government acted to facilitate trade with the USSR, the response of US private industry is uncertain. It would obviously depend in the first instance on the profitability of specific deals. Even so, many US importers would probably be reluctant to switch from established sources of supply, especially in view of their uncertainty as to the permanence and reliability of the USSR as a source. Many US manufacturers would be reluctant to give the Soviets access to equipment embodying advanced technology, fearing that the Russians would choose to compete in third country markets. Others, feeling that trade with the USSR would be sporadic and risky, might be reluctant to undertake the retooling and plant modification necessary to meet Soviet specifications. Finally, American private business often foresees public relations difficulties in trade with the USSR, even though the transaction may

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be entirely legal, and therefore would probably move cautiously in the matter.

13. As to the permanence of Soviet desire for expanded trade with the US and other advanced countries, pre-1941 performance suggests that the fear of a one-shot operation, or at least of highly irregular Soviet levels of demand, is well-founded. Khrushchev's offer emphasized the Soviet desire to buy plant, equipment, and technology rather than finished products, and it may be that in many areas the Soviets would proceed to produce their own and not draw further on the West. However, it appears likely that the West will continue to develop a variety of processes attractive to the USSR; imports of Western machinery would also, as a practical matter, ease the pressure which growing internal development and demands from other Bloc countries have placed on Soviet machinery and equipment industries. Hence, the aggregate of Soviet demand for machinery and equipment should continue and even grow at a fairly steady pace. Moreover, while the Soviets still adhere basically to a doctrine of self-sufficiency, they have in fact attained this goal in virtually all key sectors of the economy, in terms of capacity for emergency purposes, and can thus afford to accept a degree of dependence on the West in non-critical fields. Thus, there may be a continuing growth in Soviet willingness to buy finished products from the West.

14. In view of these conflicting factors, it is clearly impossible to make any firm prediction of the extent to which US trade with the USSR might realistically be expected to increase. For the purposes of this paper, we believe it reasonable to assume that if the US encouraged such trade by taking administrative action to liberalize export licensing policy and to minimize import discriminations, exports to the USSR might expand to about $100–150 million annually over the space of the next few years. This figure reflects an estimate of Soviet requirements for imported machinery in light of their Seven Year Plan, and a consideration of the possible magnitude of Soviet exports to the US.[1] While the USSR would probably not be able to balance trade at this level by its own direct export of goods to the US, it could make up the residual amount by reexports, transfers of free exchange, and by selling more gold to the Free World. This assumption of a trade expanded to $100–150 million does not allow for an increase which might occur if US credits and MFN tariff treatment were made available to the USSR — developments which would require legislative rather than merely administrative action.

III. EFFECTS WITHIN THE BLOC OF INCREASED US-USSR TRADE

A. Economic

15. Should the USSR import machinery and equipment from the US in approximately the assumed amounts, it would of course gain certain advantages. We cannot, however, give any exact estimate of the size or extent of these advantages. The total value of the imports — $150 million — is an insignificant percentage of the total value of Soviet domestic production of machinery and equipment — $25 billion. Moreover, the net gain to the USSR would be but a small proportion of the $150 million, since the imports would have to be paid for by exports drawn from the Soviet domestic economy. It is clear, however, that the advantages accruing to the USSR would be greater than these figures indicate to the extent that the Soviet imported complete plants of advanced design, or types of machinery and equipment they themselves had never produced. Such imports would permit savings of development capital and of the time of relatively scarce trained personnel. By importing complete plants, the USSR could reduce the time needed to reach a full production run.

16. The effects of increased trade in terms of output of specific industrial categories or of specific commodities would depend wholly on decisions made by the Soviet leaders. Soviet leaders would be able to use the new equip-

[1] See annex, *Possible Size and Composition of US-Soviet Trade.*

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ment either to increase output or to reduce the cost of production at the existing level. The Soviet leaders would also, in some cases, have the option of using the imported machinery either to facilitate an expansion of consumers goods production or to increase output of commodities for use in more basic industries. Importation of plant for the petrochemical industry would assist Soviet efforts to shift from agricultural products to petroleum as the principal source of raw materials for the production of synthetic rubber, alcohol, and other chemical products.

17. With respect to military production, we assume US export controls will prevent the movement to the USSR of strategic commodities. On this basis the increase in trade projected in this estimate would have slight effect on the Soviet military potential. However, improvements in the chemical and synthetic industries, for example, would make for some additional flexibility in the range of materials available for military production and might cut the costs of production of these or other items.

18. Increased trade with the US, of the assumed level and character, would have little effect on Soviet trade with the underdeveloped countries or with the rest of the Bloc. The bulk of Soviet exports to these countries consists of arms and military equipment, raw materials, and basic industrial machinery and equipment; it does not include technologically advanced equipment of the type which the Soviet Union apparently hopes to obtain from the US.

B. Political

19. The postulated expansion of US-USSR trade, by itself, would probably have little or no impact on the attitude of Soviet leaders or of the Soviet public toward the US. Even if the gains from this increased trade were turned largely toward improving the Soviet standard of living, the USSR's own contribution to such a program would be so large that the US contribution, even if publicly admitted, would be almost completely overshadowed.

20. We do not believe that an increase of trade between the US and the USSR would have any appreciable political or economic effect upon the European Satellites or upon Communist China. The governments of the European Satellites might, if they saw US-USSR trade expanding, seek to increase the trade of their own countries with the US, and they would probably expect neither the US nor the USSR to pose any insuperable political objection to such an increase. Some of the people of the European Satellites might be discouraged by evidence of improving relations between the US and the USSR; we believe, however, that such an effect would not be of long-term significance.

IV. EFFECTS ON THE NON-COMMUNIST WORLD OF THE INCREASED US-USSR TRADE

21. From a political point of view, most non-Communist countries would probably welcome the prospect of an increase in trade between the US and the USSR. They would view it as a sign that world tensions were relaxing, and that the danger of war was lessening. Many of them would consider that the US had come around to a more realistic trade policy. At the same time, it is virtually certain that some elements in many countries, and the governments at least of South Korea and Nationalist China, would regard the development as signifying another capitulation by the US to the USSR. The Japanese government would be highly resentful that the US government had changed its own policy after pressing the Japanese to move cautiously in their trade with the Bloc and to minimize their political and economic relations with Communist China. Many underdeveloped countries would be even less willing than they are today to listen to US warnings concerning the dangers of expanding economic relations with the Bloc. Reactions would be affected to a considerable extent by the timing and handling of the US move and the circumstances of the international situation. But in the final analysis, the view taken by most countries would depend largely upon the impact which the increase of US-USSR trade had upon the trade of these countries.

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22. Should the US export to the USSR the types of goods which we discuss in the Annex to this paper, it would find itself in competition with Western European and perhaps Japanese exporters. If this competition led to a reduction of presently existing levels of Western European or Japanese exports to the USSR it would certainly become an irritant in US relations with the countries concerned. It is probable, however, that the total amount of Soviet imports from the non-Communist world would increase sufficiently to allow not only for the projected increase in imports from the US, but for an increase of imports from other countries as well. Moreover, the US is now in competition with Western European exporters in many third areas without giving rise to serious political problems. We believe, therefore, that increased US exports to the USSR would not lead to significant political difficulty with other non-Communist countries. Nevertheless, it is possible that irritations could arise from this cause, especially if the general level of trade in the Free World was low. There might also be certain particular lines of US exports which would displace the corresponding lines of certain other countries. Finally, the possibility cannot be excluded that the USSR itself would deliberately take US goods and exclude the goods of certain other countries in order to cause friction in the Western alliance.

23. As for US imports from the USSR, some countries selling to the US would be adversely affected by competition of Soviet raw materials in the US market. There would be minor reductions in the dollar earnings in some cases, but at the levels of US-Soviet trade we have postulated the effect would in general be small. It would be necessary to consider, however, whether a substantial increase in US imports of some specific commodity from the USSR might seriously damage the trade or the foreign exchange position of some particular Free World country. For example, substantial US imports of manganese from the USSR might displace imports of the same commodity from India, and imports of forest products from the USSR might displace those from Scandinavia. The degree of such displacement, and its political and economic effects, could only be judged after study of the particular commodities involved and of the trade patterns which would be disturbed.

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ANNEX

POSSIBLE LEVEL AND COMPOSITION OF FUTURE US-SOVIET TRADE

A. Level of Trade

In recent years Soviet imports of machinery and equipment have probably averaged six to seven percent of the domestic production of these goods. (See Table I.) Assuming that the ratio remains roughly the same, Soviet imports of machinery and equipment in 1962 from other Bloc countries as well as from the Free World would amount to about 2 billion dollars, more than twice their present volume. However, in part because of increasing Chinese and underdeveloped areas demand for European Satellite machinery exports, the USSR in the future will probably purchase a higher proportion of its machinery and equipment imports from the Free World. In these circumstances, it is not unlikely that by 1962 Soviet imports of machinery and equipment from the Free World could increase to about 30 percent of the total import of such goods or approximately $600 million, as compared to about 25 percent in 1956. (See Table II.) Of estimated total imports from the Free World in 1962, it is assumed that not more than 25 percent, or a maximum of $150 million, would come from the United States — this would amount to an increase in the relative importance of Soviet imports of machinery and equipment purchased in the US from one percent to 20–25 percent of total imports of such goods from the Free World.

TABLE I

SOVIET INVESTMENT, PRODUCTION AND IMPORTS OF MACHINERY AND EQUIPMENT 1955–57 AND 1962
(Billions of 1955 dollars)

Year	Investment	Production	Imports	Import as a percent of Production	Import as a percent of Investment
1955	12.2	11.9	0.9	8	7
1956	15.5	15.2	0.9	6	6
1957 p	17.3	17.1	1.1	6	6
1962 *	25.0–28.0	24–26.3	1.5–2.0	6–7	6–6

p — preliminary
* — estimate

TABLE II

SOVIET IMPORTS OF MACHINERY AND EQUIPMENT
(In million US dollars and percent of total)

	1955		1956		1962	
	Value	Percent	Value	Percent	Value	Percent
Sino-Soviet Bloc	744	80.4	666 *	74.4 *	1,400	70.0
Free World	181	19.6	229	25.6	600	30.0
Total	925	100.0	895	100.0	2,000	100.0

* The decreasing share of the Satellites in total Soviet imports of machinery and equipment was undoubtedly accelerated in 1956 by the economic dislocations of the East European revolts.

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B. Composition of Trade

Although Khrushchev made only the most general comments concerning the commodity composition of an expanded trade, we believe that on the basis of known Soviet priorities during the forthcoming Seven Year Plan the following would constitute a reasonable estimate of the major categories of goods involved in the trade.

Percent of total

1. *Soviet Imports from the US*

20–25% Iron ore processing and steel rolling mill plants and equipment: The USSR has need for such equipment to relieve the strain on the already overburdened machine building industry and it is generally conceded that US has technological superiority in iron ore processing.

20–25% Chemical processing plants and equipment: The low technological level of the Soviet petrochemical industry and plans for its substantial development by 1965 assures a relatively high priority to such imports.

15–20% Refrigeration and food processing equipment: The use of refrigeration equipment for the chemical and food industries (both of which are scheduled for considerable expansion by 1965) and US superiority in this field rank such equipment high on Soviet shopping lists in the US.

10–15% Equipment for production of synthetic fiber and for the production of yarn, fabric, and clothing from natural and synthetic fiber: Soviet interest in such equipment is undoubtedly motivated by desire to improve Soviet standard of living. Although orders for such equipment would more likely be placed in Western Europe, the USSR has already exhibited an interest in purchasing US textile plants.

10–15% Metal cutting and forming machine tools; mining and construction machinery; timber, pulp and paper producing plants and equipment; miscellaneous consumer goods, possibly including foodstuffs.

2. *Soviet Exports to the US*

20–30% Ferroalloys, ferroalloy ores, and concentrates: The United States has traditionally been a major importer of Soviet ferroalloy ores and concentrates. In the pre-war period, for example, more than 25 percent of total Soviet manganese exports were purchased by the US. Presumably, Soviet exports of manganese and chrome ores could again be expanded to meet any increased US demand. However, because of the hiatus in Soviet-American trade during the 1948–58 period, any resumption of large US purchases would entail a shift from now well-established sources of supply located primarily in underdeveloped areas.

20–25% Coal tar chemicals and petroleum products: Benzene has accounted for approximately 40 percent of Soviet exports to the US in recent years. However, because benzene is consumed in the production of synthetic organic chemicals, production of which will rise rapidly in the USSR by 1965, it is expected that total Soviet benzene exports will tend to level off, if not decline, by 1965. Petroleum and petroleum products, however, will continue to be the most readily available of all Soviet potential exports.

10% Furs and forest products: Traditionally a large item in Soviet exports to the US, in recent years fur exports have fluctuated between 30–60 percent of the total, and presently amount to about $4 million. It is estimated that exports in this group could amount to about 10 percent of the total in 1962 ($10 to 15 million).

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15% Precious Metals (other than gold) (5%), cotton linters and waste (5%) and miscellaneous (5%): Platinum and platinum group metals, like cotton linters and waste, have each averaged approximately 5% of total US imports from the USSR. There is little likelihood that given the absolute increases provided in an expanding US-USSR trade, their relative shares in such trade would measurably increase.

15–30% Residual: A Soviet net import surplus from the US could be settled by means of gold sales, sales in the US of commodities purchased from third countries, or credits. Soviet gold resources are estimated to be adequate to meet a residual on this order of magnitude.

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